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Master's Thesis of Public Administration

**The Impact of Foreign Concessional Loan on
the Government Incumbency:
The Case of Mongolia**

**양허성 차관이 정부의 재임기간에
미치는 영향:
몽골 사례를 중심으로**

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The Case of Mongolia

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Abstract

The Impact of Foreign Concessional Loan on the Government Incumbency: The Case of Mongolia

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This thesis seeks to find the causal relationship between a foreign concessional loan and the government incumbency for the case of Mongolia. As a result, using multiple regression analysis, the causal relationship between two variables showed positive result which indicates that the increase of concessional loan makes the incumbent government stay longer. The conclusion is that the government borrows more concessional loan from donors to stay longer in power and use the foreign loan sources to finance the projects which are in line with their political interests.

Additionally, the literature review explains the facts that some projects financed by foreign concessional loan are inefficient and the ODA is not an effective tool for economic growth and the development of the country. The reasons for inefficiency are that donor countries have their own economic interests and target the ones according to their needs. Also, the allocated financing is not used efficiently where it is needed and recipient countries buy products at higher prices, which makes ODA project results inefficient

at the end.

Not only inefficiency, I discussed negative impacts of ODA in the thesis. The worst is a debt trap which has become an important issue for developing countries recently, including Mongolia, because many developing countries fall into a debt trap due to its inability to repay their debt back to the donor country. Due to the poor ODA policy created by the government, countries' external debt increases sharply and sovereign countries are facing reconsideration of their independence.

**Keywords: Official Development Assistance (ODA),
Concessional Loan, Government Incumbency, Government Debt**

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LIST OF ABBREVIATIONS

| | |
|------|---|
| ADB | Asian Development Bank |
| BRI | Belt and Road Initiative |
| CPI | Consumer Price Index |
| FDI | Foreign Direct Investment |
| GDP | Gross Domestic Product |
| IDA | International Development Agency |
| MNT | Mongolian Tugrug |
| MOF | Ministry of Finance |
| NSO | National Statistics Office |
| ODA | Official Development Assistance |
| OECD | Organization for Economic Cooperation and Development |
| PPP | Public private partnership |
| PRC | People's Republic of China |
| UK | United Kingdom |
| USD | US Dollar |
| WB | World Bank |

CHAPTER 1. INTRODUCTION

This chapter describes the structure of study, including the background, problem statement and the research purpose.

1.1. Background

The modern history of Mongolia started when Mongolia declared its independence in July 11, 1921 after the fall of Qing Dynasty¹ in 1911 and established the unitary socialist sovereign state, the Mongolian People's Republic, in 1924 with the participation of Soviet Union². Thenceforward, in the following years, Soviet power took place and Mongolia encouraged communism within the country for almost 70 years. There was only one political party, the Mongolian People's Party, in power until the year of Soviet Union dissolution had started.

In 1990, Mongolia had a democratic movement headed by young politicians against Soviet rule as other countries had s disintegration with Soviet Union. As a result, the movement was successfully led to a democratic revolution, the amendment of the Constitution, legalization of new political parties,

¹ Mongolia had been under control of Manchus, who later established Qing dynasty, since 1691 for more than 200 years.

² After the fall of Qing Dynasty, Republic of China was also established and Chinese called themselves the successor of Qing Dynasty. Chinese tried to occupy Mongolia, however, Mongolians got military help from Soviet Union and could declare its independence.

establishment of a standing legislative body and creation of an office for the president. The very first parliament election after the democracy was held in 1992 in Mongolia and adopted a new constitution which was subject to lead to democracy and prosperity. By the new constitution, the People's Republic was abolished from the name of the country.

Mongolia's transition from communism to democracy and a single-party authoritarian system to an open market economy had brought a huge opportunity for further development of the country. Even though Mongolia had some rough relations with both neighbors, Russia and China, in the past, the priority is always to maintain friendly and balanced relationships with them in the future.

Currently, Mongolia can be described as country with a semi-presidential system because the president is elected directly by the citizens, and has extensive powers such as, initiating legislative bills and appointing Supreme Court judges, issuing guidelines for the government, and heading the National Security Council. The president is the head of the country and is chosen by four-year terms.

The prime minister is the head of the government, however, the parliament of Mongolia has all legislative power. The party who gets the most seats in the parliament forms the government and confirms the appointment of the prime minister and cabinet members. The parliament has the power to

declare states of emergency and war, ratify international treaties and agreements, enact and amend laws, draft legislation, approve the annual budget and foreign and domestic policies. The parliament is consisted of 76 members who are chosen by the majority vote for four-year terms. Since 1990 until today, Mongolia had 7 parliament elections and 18 governments including the current one. Basically, throughout the times, the Government had changed approximately 2 times in one parliament term.

There are two major political parties in power in Mongolia. The one is the oldest political party, the Mongolian People's Party which is a powerful and well-regulated political institution following the old Soviet rule, while the another is the Democratic party which is more oriented to lowering taxes, accessing to foreign direct investment, and maintaining the judiciary independence that are essential for the rule of law to be in power. Throughout the times since 1990's, these two parties are dominating in the parliament one by one. The political party who took the majority seats in parliament can affect every decision made by the government including public and foreign policies, expenditures, and investments. The common attitude of the political parties in Mongolia is usually to allocate more public expenditures and investments to their election constituencies to get more votes for their next parliament election. However, after almost 30 years had passed, the democracy of Mongolia is still in the process of developing, economy is not doing very well and people are still in poverty.

Political and public institutions are not stable and corruption took place everywhere. Fractions and populism within political parties and within the Government had been increased and two major parties always fight with each other even though they tried to form coalition governments few times already.

Mongolia had faced substantial economic challenges in the first years after the transition in the 1990s from communism to democracy. The economy was thoroughly dependent on foreign loans and aids to recover from the downturns. Official development assistance (ODA) was the most essential tool to strengthen economic growth and the political situation, especially during the early years after transition. In the early 2000s, Mongolia had taken significant actions toward the establishment of more contemporary and strong economy, based upon its mining sector.

Mongolia has a huge deposits of coking-coal, gold, uranium, and copper. There are few big mining companies, but to highlight the Oyu-Tolgoi and Tavan-Tolgoi are the ones which are always on attention of everyone, local and foreign. Oyu-Tolgoi which started its operation in 2010 is the single largest project in the world for mining gold and copper while Tavan-Tolgoi is the largest undeveloped coal mine in the world. The first investment of \$5 billion for Oyu-Tolgoi was made in 2011 by foreign investors and procurement for contractor was finalized at Tavan-Tolgoi at the same year.

Due to those good news, foreign investors rushed to Mongolia seeking investments not only in mining sector. The economy of Mongolia reached at its peak with gross domestic product(GDP) growth to 17.3%, driving double-digit economic growth, in 2011 from 6.4% in 2010, and since then the economy had sustained to grow twice a more for years³ (Monitoring Profile of Mongolia-2016, 2016). This growth from the mining sector had an enormous influence on the expansion of other sectors, including infrastructure, information and communication technology and energy. During this period, foreign direct investment and foreign trade have taken place of foreign loan and aid.

Although, this glee had ended soon and the recession had pushed Mongolia, the natural resource and mining dependent country, in challenging circumstances during 2014 to 2016. The cause was driven by a decrease of commodity price in the world, especially in People's Republic of China which is the largest export market of Mongolia covering about 84% of whole exports since 2005. About 80% of Mongolia's export⁴ consists of minerals and 68.4% of the mining exports went to the People's Republic of China (PRC) (NSO, 2018).

Thereby, the slowdown in the economy of PRC had given negative impacts,

³ The detailed graph of GDP growth rate is shown in APPENDIX A.

⁴ The detailed export information by country and product type is shown in APPENDIX B.

and economic downturn after the mining boom has brought the following knock to the economy of Mongolia:

- The large deficit, along with Mongolian currency depreciation, drove general government debt to 93.1 percent of GDP in 2016,
- Credit ratings downgraded from BB- to B-,
- FDI fell from 4.5 billion USD in 2012 (more than 40 percent of GDP) to nearly zero in 2015,
- Demand for mineral from China weakened and coal and copper export prices fell sharply,
- Higher costs of international borrowing, large financing needs and high interest rates threatened debt sustainability.

To fight with the economic downturns, the Government of Mongolia has officially brought official development assistance policy back to attention. Since that time, total official development assistance inflows, especially the concessional loan amount, have relatively been increasing and diplomatic relations with donor countries have been restored.

The economy of Mongolia is heavily dependent on mining sector. Until the mining sector, especially Oyu-Tolgoi and Tavan-Tolgoi projects start generating investment returns and giving a positive impact to the economy, the concessional loan from foreign countries and multilateral organizations would be expected to mend the economic gap and still be in demand. Hence,

Mongolia has a long journey to tolerate with development partners for many years ahead.

1.2. The Statement of the Problem

The life cycle of governments⁵ is quite short in Mongolia, with median age of 1.9 in years, since the beginning of the transition from communism to democracy in the beginning of 1990s. The making and breaking of governments has become an opaque process in Mongolia. The reasons are the following; a change in government is demanded whether on the basis of an election, a resigned government, a conflict of interest within the parties who have seats in or outside the government, or a conflict of interest within the parties who have seats in the parliament which can directly affect to actions of the government or there exists some other reasons which we do not know.

Each government tries to survive longer during a four-year parliament term to fulfill its purposes and goals, and their main financial sources have become ODA which can be raised in a shorter period of time comparing to other financial sources. Official development assistance; especially concessional loan from development partners, has been in demand in Mongolia since 1991. Until 2011, a foreign concessional loan has been a

⁵ The detailed incumbency information of Government of Mongolia is shown in APPENDIX C.

major external financial source for the government and, in 2012, the Government of Mongolia had issued its first external bond named “Chinggis”. Since then, several external bonds have been issued including, the Mazaalai bond, the Samurai bond, and etc. Due to the high prices which are based on the market and the economy of the country, bonds⁶ are more expensive and the repayment period is shorter comparing to foreign concessional loans. Thus, foreign concessional loans, of which the interest rate ranges between 0.15%-3% with 13-50 years of repayment period, are still a demanding external source for the Government of Mongolia.

Even though there is a geographical advantage in Mongolia located between two huge markets, China and Russia, the internal fights within political parties are blocking the further growth in mining sector. Foreign investors lost their confidence because of political instability caused by political party interests and the environment for foreign direct investment has become not favorable anymore. The huge deposit of natural resource still untapped underneath the ground and it is taking long time for mining sector to give its fruits to the economy.

Due to the high expense and the long period to raise other financial sources, the only best option for government has become borrowing loan from

⁶ The interest rates of external bonds range from 1.5% to 7.5% and the repayment period is 3 to 10 years.

development partners in concessional term.

However, on the other hand, the government debt⁷ which is one of the important indicator for economic development, has been increased from 26.7% in 2011 to 93.1% of GDP in 2016 reaching at its highest in 10 years (MOF, 2018). Borrowing cheaper sources from our friends might be good short-term solution for implementing development plans, however in other thoughts, question for what worse can happen due to the increasing number of government debt in the future is raised.

Therefore, this thesis seeks to analyze what impacts the foreign concessional loan have in the long term, how it affects for the government activity and to define whether the increasing amount of concessional loan affects the incumbency of the government due to the many number of changes in the government for the past 29 years.

1.3. Purpose of Research and Research Questions

This research will focus mainly on determining, examining and analyzing the increase of ODA, more specifically the concessional loan which affects the sharp growth for government debt, and whether it affects the government itself to shake from the ground.

⁷ Government debt is how much the government owes to the creditors outside the government itself.

Also, this research aims to elaborate key issues related to the trends towards the increasing number of concessional loan amount from year to year and what impact it can bring to the country in the long run.

The research question that this study aims to answer is the following:

1. Does foreign concessional loan affect the duration of the government in Mongolia during the last 29 years? Does foreign concessional loan affect government incumbency in a positive way or more to the negative way?
2. What is the long- term impact of concessional loan to the developing country like Mongolia? And what are examples of consequences and impacts of ODA to recipient countries which borrowed high number of concessional loans from foreign countries?

The research objective is not only determining the impact of concessional loan to the incumbency of the government, but also to define the positive and negative impacts of ODA to the economy and society using the case of Mongolia and to raise further awareness, as well as to contribute to the empirical study of ODA and its impact.

This thesis proceeds as follows: Chapter 2 of this thesis provides literature review, Chapter 3 includes detailed methodology of the study and Chapter

4 discusses the research findings. The final chapter 5 addresses conclusion including, summary of findings and policy implications.

CHAPTER 2. REVIEW OF LITERATURE

The purpose of the literature review is to have a basic theoretical understanding of definitions of the main concepts and to have a knowledge of background on the facts. Hence, the literature review is more descriptive and comprehensive. Precedent studies concentrates not only on scientific journal articles but also studies from international organizations and researches which is basically practitioner-oriented.

In this chapter, I first will determine the conception of government incumbency and how political power affects the incumbency of the government. Next, how incumbent government can affect to the society and the economy, and what relationship the government and ODA have, will be discussed. Afterwards, the ODA and its purpose will be explained. At the end of this chapter, I include and discuss the causes and consequences of the borrowing concessional loan, and how ODA affects and give impacts to the recipient countries.

2.1. Government Incumbency and It's Driving Force

The government is consisted of members of the political parties who took the majority seats in the parliament. Political parties usually have three main goals: vote seeking, policy seeking and office seeking according to the article of Hans Keman (Keman, 2011). The first goal represents

behavior of parties with respect to the electorates in maximizing their presence and degree of dominance in parliament. The second goal is to direct government what is in the party's interest and reflects their ideas how society ought to be shaped by means of policy formation. The third goal is gaining access to the executive by competing with other parties for office. These are the participation of political parties in government. Political parties are the ones who make policy choices and control the government action (Keman, 2011). The argument, Keman made is that the composition and survival of a government has become more and more the result of parties' behavior aiming at incumbency, and thereby neglecting by and large whether or not the actual political course of action or policy-seeking behavior of government is more or less responsive to electoral preferences. Rather than being a party that is a mediator between state and society, the behavior of political parties change and it appears that parties and their leadership tend to become part of the 'state' only not the representative of the voters but to seek the offices.

There are different types of political parties depending on their power in the parliament. A central party is that the party that is the one in between left-right and progressive-conservative distribution of a party system. A dominant party is the one with most seats in parliament (Roosendaal, 1992). Obviously, parties being both central and dominant, pivot parties, play a crucial role in forming and running government and making public policies.

This implies that non-pivotal parties remain more dependent on other parties to prolong their incumbency successfully. Once a party has achieved a pivot position, it is more likely to stay in government for longer periods. According to the study of Keman, average government in Europe lasts 2.3 years which is not very that far different from Mongolian case, while the world average is 3.7 years.

The reasons for termination of governments, vary depending on different constitutions of each country. It can be electoral ones to conflict within government or parliament. According to Laver, early empirical studies have shown that a government that is ideologically compact, with a single-party majority cabinet or minimum winning coalition, in a party system with low fragmentation and subject to a formal investiture requirement is predicted to last a longer than an ideologically diverse minority coalition in a fragmented party system with no investiture requirement (Laver, 2003). Researchers also concluded that governments exist in a world of critical events, such that scandals, international conflicts, financial and monetary crises, the deaths and illnesses of key personalities, each of which poses a threat to the life of the incumbent administration (Laver, 2003). But those critical events can be occurred due to the interest of political parties or the policies introduced by the government itself.

The change of government and the policies is a sign of political instability

as described by the researchers, Alesina et al, Gasiorowski, and Miljkovic and Rimal. Hence, they defined political instability in several ways. The most common are the following: to define it as the propensity for regime or government change, the incidence of political upheaval or violence in a society, such as assassinations, demonstrations, and instability in public policies and so forth. Just as there are a number of definitions of political instability, there are also a number of indices designed to measure the level of political instability in countries. The most commonly used indices are POLITY indices and the World Bank governance indices (WGI) in academic and policy use.

2.2. Government Incumbency and the Socio-Economy

The economic growth and the political stability are very much interconnected. (Hussain, 2014). On the one hand, the uncertainty associated with an unstable political environment may reduce investment and the pace of economic development. On the other hand, poor economic performance may lead to government collapse and political unrest. For example, in the country like Mongolia with short government incumbency, the likelihood of a government change has a larger effect on the degree of uncertainty in the economic environment and the higher the degree of political polarization in society. Basically, the stable politics affects positively to the economy of the country.

Furthermore, political stability has impact on the increase of government efficiency. If government or policies change frequently, inefficient institutions can arise and persist and it can make the whole society unstable. According to the social conflict view, economic and political institutions are chosen by the groups that have political power at the time and they will make the changes within the institutions and choose policies that will maximize their own rents rather than benefiting the whole society. For example, Acemoglu and his colleagues stated in the article that political parties currently incumbent establish the economic institutions which will lead to different distributions of resources according to their needs (Acemoglu, D., Gallego, F.A. and Robinson, J.A, 2014). This will result in inefficiency for the government performance due to its lack of resource needed for certain groups.

The economy may do well in terms of attracting foreign direct investment because stability means a predictable political environment and any more. However, there are also negative sides of political stability. Other aspects of the society might suffer because of lack of competition, complacency, and opacity due to the longer duration of a single government. Consequently, stability of the government does not necessarily lead to higher economic growth. India is a case in point. India's performance on the economic front in the first 30 years of post-independence era, which epitomized political stability, exhibited 3 to 3.5 percent level of economic

growth, lowest in the last sixty years. In contrast, in the last 20 years when India saw as many as four Prime Ministers, industrial growth rates jumped to double digits, something that had not happened before (Hussain, 2014).

Moreover, according to the World Bank report, political stability not only prevents any possible changes, but this can discourage the public. People look for changes in every public sectors to have a better development. Stable politics with the incumbent government which lasted for a long period decreases the chance of a competition which can lead to a corruption and the abuse of power in public sector. The principles of competition not only applies to the market. It also applies to every public sectors.

So that, there are positive and negative sides for political stability, more specifically for the longer staying incumbent government. If so, according to the interest of this study, how incumbent government affects ODA or reverse impact will be discussed in the next sub-chapter.

2.3. The Government and ODA

When the power of Government is extensive, the fight for political power intensifies the resulting political tension. The result is that the energies and activities of citizens are shifted from economic activity to political activity. Bauer notes that the political effects cannot be simply observed by the commonly used statistics on the size of the government sector. There can

be the case where the government has more control over the expenditures focusing on providing the basic services for the citizens rather than being much involved in caring the economy. However the allocated government financial source is limited and government opens its arms to donors. So that, the ODA source somehow is used to finance the need of government in political reasons. Bauer mentions that “foreign aid is neither a necessary nor a sufficient condition for advance from poverty” but the countries become “dependent on large-scale foreign aid and gifts of food” with no significant rise in living standard (Bauer, 1969). Friedman argues that if ODA is allocated to help a group with political power for overcoming their political crisis during short term and letting them keep the political power may cause negative political effects. (Friedman, 1958)

Moreover, there is a study noting that the bureaucracies of governments in developing countries can be weakened by the ODA (Knack, 2001). The research suggests that more opportunities to design and implement projects financed by ODA should have been given to recipient governments, however, as a result, administrative capacity of the government increases extensively. The study of Remmer, with respect to government expenses and aids, also showed the same result that dependence on ODA encourages the expansion of government size in middle and lower income countries (Remmer, 2004). Rajan and Subramanian tested a hypothesis that aid may undermine the quality of governance using World Governance Indices and the result

showed that the increase of ODA is related to the weak governance (Rajan, R. G., Subramanian, A, 2006). As a production of government, public policies are vital for growth of the country. Burnside and Dollar investigated the relationships between ODA and institutions and policies that have direct impacts on growth, and the result of the study was that aid spurs growth with better institutional quality were more robust (Burnside, A. C., Dollar, D, 2004).

To conclude, ODA is an effective tool for the government in terms of growth in many sectors if government takes the smart measures related to the ODA policy. Otherwise ODA might be as dangerous as the enemy to the government. Before studying deeper into the causal relationship between government incumbency and the ODA, let's discuss what ODA is in detail for the next sub-chapters.

2.4. The Fundamental Determinants of ODA and its purpose

There are several external financial flows as described by OECD. These flows include: (i) remittances, (ii) private flows at market terms, including foreign direct investments, and total bank and non-bank purchases of bonds and other securities, including equities, (iii) private grants, (iv) non-concessional source from multilateral and bilateral development partners

that do not meet the requirement of ODA and (v) concessional financial source from multilateral and bilateral development partners that meets the requirement of ODA.

As described by OECD, concessional loans are loans that are cheaper than the market based loans and have longer period for repayments. The interest rate is also below the market value and grace period is longer than any other types of external financial sources.

Development Assistance Committee, one of the organizations of OECD, has defined Official Development Assistance as follows:

“Flows of official financing administered with the promotion of the economic development and welfare of developing countries as the main objective, and which are concessional in character with a grant element of at least 25 percent (using a fixed 10 % rate of discount). By convention, ODA flow comprises contributions of donor government agencies, at all levels, to developing countries (“bilateral ODA”) and to multilateral institutions. ODA receipts comprise disbursements by bilateral donors and multilateral institutions. Lending from export credit agencies—with the pure purpose of export promotion—is excluded.”

In the paper of Antonios Balaskas, Eduardo Lima and Tyler Seed, ODA is classified into two types, bilateral and multilateral, depending on who provided. Bilateral ODA is development assistance conferred on a recipient country by a donor country (Antonios Balaskas, Eduardo Lima, Tyler Seed, 2009). The distribution of ODA by a donor country is usually managed by that country's international development agency. These agencies are attached to a greater or lesser extent to the government's ministry or

department of foreign affairs. Examples of bilateral ODA agencies include the Japan International Cooperation Agency (JICA), Korean International Cooperation Agency (KOICA), the United States Agency for International Development (USAID), etc. Multilateral ODA is conferred on a recipient country by an international organization drawing on a pool of financing from a variety of donor countries. These organizations may be multi-purpose international organizations such as the World Bank, Asian Development Bank (ADB) and the United Nations Development Program (UNDP) or thematic/sector specific organizations such as the United Nations Children's Fund (Antonios Balaskas, Eduardo Lima, Tyler Seed, 2009).

According to Antonios Balaskas, Eduardo Lima and Tyler Seed's paper, there are several powerful incentives exist for developed country governments to become active donors. These very pragmatic and interconnected motivations include political and economic benefit, national security, better immigration control, expectations of the international community, popular public sentiment among its electorate, and global climate security. Also, in another article of Axel Michaelowa and Katharina Michaelowa, it is concluded that while poverty eradication has been officially set up as the central objective of aid, this does not necessarily imply that donors act accordingly. In fact, ever since the late 1970s, a large and growing amount of empirical literature on the geographical distribution

of aid has clearly established that donors strive for a multitude of different objectives. Aims such as export promotion, political and cultural hegemony, etc. are frequently given priority over recipients' needs. The reasons can often be found in the political economy of individual donor countries: bureaucratic procedures which create incentives to spend a maximum amount of money within a restricted budget year, electoral processes which cannot be won with the objective of international poverty reduction, and lobbying by private firms that regard aid as an interesting pool for indirect subsidies (Axel Michaelowa, Katharina Michaelowa, 2007). This type of indirect purposes are usually brought by bilateral donors because multilateral donors establish their goals in a comprehensive manner, and their monitoring and control is quite strong comparing to bilateral donors due to the participation of multiparty and many countries.

The fact is that aid in a bigger portion was used in achieving donors' own interest rather than accomplish the main purpose to contribute for the progress of developing countries in meeting their basic needs, reduce poverty or any other tangible improvement in poor's people live. In this case, the question comes up that whether the ODA was effective or not for the recipient countries at the end of implementation.

2.5. Effectiveness and Impact of ODA to Recipient Country

Much of theoretical and empirical literatures have investigated the economic and social effects of ODA. Some empirical studies proved a positive impact of ODA on the economic and social growth of the recipient countries (Burnside, A. C., Dollar, D, 2004). Asteriou performed analysis to check the relationship between ODA and economic growth. He used a panel data set from 1975 to 2002 for five South Asian countries; Bangladesh, Nepal, India, Sri Lanka, and Pakistan. The research provided robust evidence of a positive effect of ODA on GDP growth (Asteriou, 2009). Jung & Lee also studies with the panel data of 41 developing countries from 1970 to 2010 and found the result that GDP has made a positive impact on ODA in the short term, and vice versa (Ki Hun Jung, Choong Lyol Lee, 2011). Moreover, Dalgaard and Tarp's study explored the empirics for the claims with respect to the effectiveness of aid in the long term. The results implied there is a strong interaction between policy and aid. Further, the results reveal that aid can play a conducive role and have a positive impact on improving productivity in developing countries (C, J., Hansen Dalgaard, F Tarp, 2004).

Yet there are many positive impacts and effects of ODA to the recipient countries, many empirical studies shed light on ineffectiveness of ODA.

Moyo stated that ODA was provided for several decades to poor countries, but unfortunately the result showed very little or non-growth in developing regions around the world, especially in Africa (Moyo, 2009). Basically it can be assumed due to the lack of effective aid. In this sense, people concern about the low impact of ODA and bring up debates in the international community about ODA effectiveness.

Therefore, a new aid architecture was introduced to the international system to tackle down those issues and in 2010, the OECD Working Party on Aid Effectiveness remarks that the widespread promotion of development was not only about amounts of aid given, but also and more important about how aid was given (Mendez, 2017), which in other words is related to the alignment process, on how donors and recipient countries interact each other and how donor's aid is distributed and recorded in the recipient country. It is not just matter of ownership where the main responsibility relies on the recipient country or harmonization where donors coordinate their activities to reduce fragmentation of aid in recipient countries. Alignment is more comprehensive, in other words means coordinated participation of donors and partners, which is the main importance of alignment implementation to make aid flows more effective (Mendez, 2017).

However, even the alignment and cooperation between donor and a

recipient has improved, ODA sources are not allocated according to the needs of recipient country but the need of a donor country to support their own economic development. For example, Eun Mee Kim and Jinhwan Oh did a research on whether donor countries allocate their sources according to the recipient countries' needs and included the example of South Korea in their article. In the study, they classified recipient 154 countries into three parts based on their income: high, middle and low income countries. The first result of the study was that South Korean ODA was focused more on the higher-income developing countries with higher growth rates. More precisely, donor country's interest was more into higher income developing countries and the humanitarian approach was into lower income countries but excluding the lowest level least developed poorer countries. The conclusion of the study was that South Korean ODA allocation shows a pattern consistent with economic interests (Eun Mee Kim, Jinhwan Oh, 2012). Another example is that the ODA provided by Japan also was criticized because Japan did not dedicate much attention to the economic and social impacts of its ODA (Yamamoto, 2019) . Its approach considered only its own economic benefit. Disregarding the recipients' circumstances, Japan's ODA contributed to corruption, debt and controversial expropriations for large-scale infrastructure projects.

ODA support is brought to a country as a project-support and it already became the traditional aid modality implemented in few decades. But it has

also been criticized that because it focuses just in individual projects, which are translated in high transaction cost and short term improvements. Soubotina stated in her article that in recent decades, tying arrangements were introduced to prevent mismanagement. Tying arrangements are sets of conditions, such as those that require “recipients to purchase goods and services from the donor country or from a specific group of countries,” (Soubotina, 2000). However, this may reduce the value of aid if the arrangements are motivated by a desire to benefit suppliers of donor countries and that may limits recipients from buying at the lowest price (Soubotina, 2000). Temple also argued that purchasing advice from overseas consultants, or purchasing goods from the donors countries reduce the effectiveness of the real results of the project, because it will cost more than the price recipient country can purchase goods and services domestically or at world price (Temple, 2010). This type of phenomenon such that tying arrangements related to the procurement is observed usually by the bilateral relations depending on the donors’ interest in return of their financing.

Not only ineffectiveness of projects, there are negative consequences followed by ODA financed by donor countries. Cohen provides an example and suggests that even well-intentioned actions have consequences that are difficult to predict (Cohen, 2006). He took an example in his article saying

that the French colonialists used DDT⁸ to combat malaria and typhoid, and built a road to address the region's isolation in a mountain village of Algeria under colonial rule. But, the unintended results were: population explosion, more intensive farming, and deterioration in the land needed to support the villagers' livestock. Due to these consequences, some people fell into poverty, others became rich and inequality increased in the country. Moreover, Seunghyun Lee and Tobin Im stated in their article that more the recipient country receives ODA, the weaker their government systems become and it promotes corruption within government (Seunghyun Lee, Tobin Im, 2015). Since these effects are irreversible, whether aid is the right solution remains questionable.

The worst consequence related to the concessional loans is a "Debt Trap"⁹. In recent example is Belt and Road Initiative (BRI) implemented by the Government of PRC. There has been a lot of hue and cry over the China's loan policy of which people call it "debt trap diplomacy" regarding African, Latin American and South Asian countries. BRI projects are mainly focused on infrastructure and scholars have argued that Chinese loans are erroneous, expensive, predatory and harmful to recipient countries (Baig, 2018). One of the example for debt trap is Maldives, the one stated in Baig's article. A

⁸ DDT is a chemical compound used for insect control.

⁹ Debt trap is a situation in which a debt is difficult or impossible to repay, typically because high interest payments prevent repayment of the principal.

report published by a Washington based think tank, which evaluated the debt implications of China's massive BRI program, concluded that the Maldives is one of eight countries that may fall prey to high debt distress from Chinese investments (Baig, 2018). The Maldivian authorities believed that the level of debt is high, yet it has been injected mainly in growth enhancing infrastructure, however, Maldives is already fallen into difficulty of repayments and 80% of Maldives debt belongs to China. If Maldives falls behind, China would ask for equity from different island-owners and infrastructure operators are likely to finally get hold of the Maldivian land. Moreover, the decision of Sri Lanka in 2018 to lease Hambantota port to China in order to reduce its BRI¹⁰ debt burden is often cited as a prime example of debt trap diplomacy as experts say (Yamamoto, 2019). In contrary to that, Chinese experts say that the investments target only infrastructure development of the developing countries, no other intention. There is no proof and evidence that China's intention is to colonize the country, but still it is not going to kill anybody to have a little concern on their ODA sources and purposes.

Meanwhile the fact is that ODA has both positive and negative economic and social impacts to the recipient country, I will be focusing deeply on the causal relationship between ODA, more specifically the concessional loan,

¹⁰ More facts on BRI projects will further be discussed in Chapter 4.

and Government incumbency.

CHAPTER 3. RESEARCH METHODOLOGY

While the theoretical issues related to government incumbency and concessional loan issues are discussed in Chapter 2, I will describe the data and the method underlying this thesis in the following section. To measure the impact of foreign concessional loan on the government incumbency, I have chosen to take the hypothesis of the research as follows:

H_0 : Concessional loan has a positive impact on the duration of the incumbent government. If government borrows more concessional loan from donor countries, it will be the factor for the extension of incumbent government.

Pure triangulation research design using the both qualitative and quantitative approach would be the underlying research method for this study to determine whether the data bases yield the similar results.

3.1. Variables and Data

Incumbency of the Government cannot be observed directly. Some governments in Mongolia lasted longer during the full 4 year parliament term, while some are changed more frequently within few months. The reason for longer staying government can be economic power which led to growth of the country or well implemented policies which led to good governance that also affects the well reputation of government. The

government change is a distinct phenomenon and I will use limited dependent variable to study the duration of the government. The dependent variable for the research will be incumbency of the government or more specifically the duration of the government in quarterly time series. The duration of government is measured using 1 to 16 scores depending on the quarters the government was incumbent within 4 year parliament term.

The independent variable is the foreign concessional loan outstanding amount by quarterly basis. Government has the power to take resources in a variety of constraints and make changes in social, economic and cultural conditions through their conversion capacity. ODA is one of the main financial resources the government of Mongolia utilizes for development purposes. The recipient governments should perform effectively to eradicate poverty and attain national development goals using the ODA sources, which at the end would strengthen the power of government and be the impact for their longer incumbency.

This study controls some other economic, social and political variables that might have influences on the degree of government incumbency. To measure and to estimate strength of the empirical relationship between government incumbency and concessional loan, party affiliation, coalition government, political stability and absence of violence index, regulatory quality index, rule of law index, consumer price index, and foreign direct

investment amount are used as control variables. Using control variables in a multiple regression analysis will reduce the risk for omitted variable bias and provide more accurate insight into the effects that concessional loan have on government incumbency.

As discussed in chapter 2, government is formed by the political parties which have majority seats in the parliament. Whether the government stays stable and incumbent will depend on the power of political party and how strong the opposition party is. So that party affiliation of incumbent government and single party or coalition government status are used as political control variables to measure the impact of concessional loan on government incumbency.

Moreover, the governance index captures perceptions of the quality of public services, the quality of civil service, independence from political pressures, and policy formulation and implementation. How well the incumbent government performed is measured by the governance index. WGI Indices including, political stability and absence of violence, regulatory quality and rule of law are used as social control variables. The governance indicator is scaled from 0 to 100. The lowest level of governance indicator is represented by the zero score, by contrast, one hundred score means the highest level of government effectiveness.

Economic situation is also the result of policies taken by the incumbent

government and it is important indicator for government performance. Consumer price index is used to capture volatility, and it is expected that lower levels of CPI will positively impact the duration of government. In addition, FDI is included as control variables to show the effective government policy on business environment.

The data collection is mainly based on the most recent data from National Statistical Office of Mongolia and the final year-end reports from Ministry of Finance of Mongolia. While the net concessional loan data is only available from 1991, I used the data set from above sources from 1991 to the end of 2018 for total 27 years. The basic data for this research are, firstly, the information of Government of Mongolia and its change throughout the times in quarterly basis, and, secondly, the amount of loan borrowed from external sources. Data set for control variables are collected from sources of World Bank, CEIG and other additional sources.

The variables and their descriptions are included in Table 3.1.

Table 3. 1. Descriptions and the Sources of the Variables

| Variable | Description | Source |
|-----------------------------|--|---------------------------------|
| Dependent Variable | | |
| Duration | Duration of the government in quarters | Gogo portal site |
| Independent Variable | | |
| Loan | Outstanding amount of concessional loan borrowed from donors /MNT billion/ | Ministry of Finance of Mongolia |
| Control Variable | | |
| Party | Party Affiliation | www.wikiwand.com |
| Coalition | Single Party or Coalition Government | www.wikiwand.com |
| Stability | Political Stability and Absence of Violence Index from WGI | World Bank Data |
| Quality | Regulatory Quality Index from WGI | World Bank Data |
| Rule of Law | Rule of Law Index from WGI | World Bank Data |
| CPI | Consumer Price Index | NSO, Mongolia |
| FDI | Foreign Direct Investment /USD million/ | CEIG data, World Bank |

3.2. The Estimation Model

To study the impact of concessional loan on incumbency of the government, the following regression equation will be used:

$$\text{Duration} = \alpha + \beta_1 * (\text{Loan}) + \beta_2 * (\text{Party}) + \beta_3 * (\text{Coalition}) + \beta_4 * (\text{Stability}) + \beta_5 * (\text{Quality}) + \beta_6 * (\text{Rule of Law}) + \beta_7 * (\text{CPI}) + \beta_8 * (\text{FDI}) + \varepsilon$$

Where:

A dependent variable-Duration of the Government,

An independent variable-Concessional loan amount

Control variables- Party affiliation, coalition, political stability and absence of violence index, regulatory quality index, rule of law index, consumer price index, and foreign direct investment

α = intercept

β = regression coefficient

Table 3.2. provides summary statistics of variables for basic simple use for the analysis. The data set covers total 112 observations for both, dependent and independent variables from 1991 to 2018. For each variable, mean, standard deviation, minimum, maximum and the number of observation are illustrated.

Table 3. 2. Summary Statistics

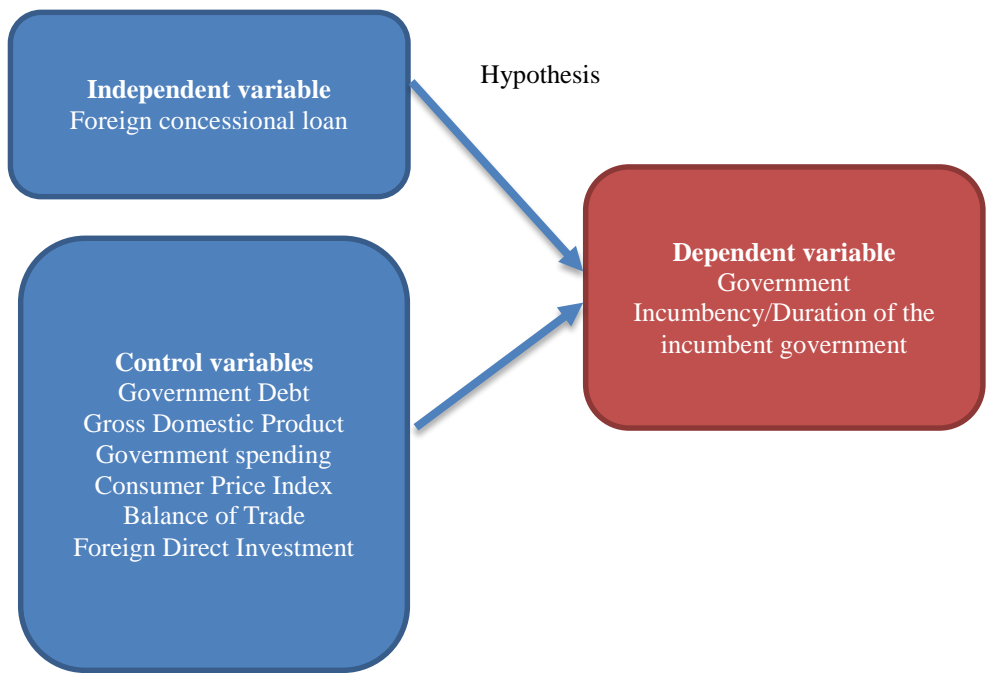
| Variable | Mean | Std Dev | Minimum | Maximum | N |
|-----------------|-------------|----------------|----------------|----------------|----------|
| Duration | 5.4196429 | 3.7695757 | 1.0000000 | 16.0000000 | 112 |
| Loan | 2140947.59 | 2402561.79 | 71.9661901 | 11201120.16 | 112 |
| Party | 0.6607143 | 0.4755949 | 0 | 1.0000000 | 112 |
| Coalition | 0.4285714 | 0.4970958 | 0 | 1.0000000 | 112 |
| CPI | 28.5885828 | 66.2705397 | -2.4573224 | 420.4171934 | 106 |
| FDI | -5.1753330 | 83.4619206 | -317.9833333 | 224.6011667 | 109 |
| Stability | 0.7022609 | 0.1864996 | 0.3529256 | 1.1715980 | 92 |
| Quality | -0.2216783 | 0.1328853 | -0.4919476 | -0.0298508 | 92 |
| RuleofLaw | -0.1375390 | 0.2315624 | -0.3797925 | 0.2130862 | 92 |

Maximum duration of the government is 16 quarters that is 4 full years, while average duration is 5.4 quarters and the lowest is only 1 quarter.

Average amount of concessional loan outstanding within the year 1991 to 2018 is 2140,947.59 MNT billion while the lowest amount is only 71.9 MNT billion nationwide.

The research model is shown in figure 3.1.

Figure 3. 1. Research framework



To prove the above hypothesis and to see the relationship between dependent and independent variables, preliminary correlation analysis has been conducted in table 3.3.

Table 3. 3. Result of the preliminary correlation analysis

| Pearson Correlation Coefficients Prob > r under H0: Rho=0 Number of Observations | |
|--|-----------------|
| | Duration |
| Loan | -0.19034 112 |
| Party | 0.32636 112 |
| Coalition | -0.17377 112 |
| CPI | -0.10657 106 |
| FDI | -0.17370 109 |
| Stability | 0.33182 92 |
| Quality | -0.22178 92 |
| RuleofLaw | 0.22972 92 |

The correlation coefficient in between duration of the government and the loan outstanding amount is -0.19 which indicates that both variables have negative correlation. Also, same correlation result is estimated for the coalition, CPI, FDI and regulatory quality. Negative correlation indicates that the increasing number of concessional loan amount and other variables affect negatively for the duration of government. However the correlation result for duration, party affiliation, rule of law and political stability and absence of violence index showed that they have moderately positive

relationship which indicates that increase of these variables affects higher possibility of duration of government. 1. Even though the correlations found to be negative, it cannot be interpreted that a variable has negative impact on another variable. Regression analysis should be carried out in order to analyze the size of influence between independent and dependent variables.

CHAPTER 4. RESEARCH FINDINGS

This chapter provides the main empirical results of the duration of government and foreign concessional loan causal relationship. The analysis is based on Mongolian economic situation and the government duration.

4.1. Results

The results show that foreign concessional loan outstanding amount has a positive impact, significant at the 0.1% level when including control variables.

Table 4. 1. Multiple Regression Analysis for Concessional Loan Impact on Duration of Government

| Analysis of Variance | | | | | |
|------------------------|----|----------------|-------------|---------|--------|
| Source | DF | Sum of Squares | Mean Square | F Value | Pr > F |
| Model | 8 | 521.97699 | 65.24712 | 7.32 | <.0001 |
| Error | 83 | 740.14257 | 8.91738 | | |
| Corrected Total | 91 | 1262.11957 | | | |

| | | | |
|-----------------------|----------|-----------------|--------|
| Root MSE | 2.98620 | R-Square | 0.4136 |
| Dependent Mean | 5.09783 | Adj R-Sq | 0.3570 |
| Coeff Var | 58.57788 | | |

| Parameter Estimates | | | | | | |
|---------------------|-----------|----|--------------------|----------------|---------|---------|
| Variable | Label | DF | Parameter Estimate | Standard Error | t Value | Pr > t |
| Intercept | Intercept | 1 | -2.64355 | 1.69852 | -1.56 | 0.1234 |
| Loan | Loan | 1 | 6.012794E-7 | 2.458321E-7 | 2.45 | 0.0166 |
| Party | Party | 1 | 2.59109 | 0.76558 | 3.38 | 0.0011 |
| Coalition | Coalition | 1 | 1.38017 | 1.72061 | 0.80 | 0.4248 |
| CPI | CPI | 1 | 0.01273 | 0.03032 | 0.42 | 0.6757 |
| FDI | FDI | 1 | -0.01416 | 0.00460 | -3.07 | 0.0029 |
| Stability | Stability | 1 | 4.45786 | 2.05085 | 2.17 | 0.0326 |
| Quality | Quality | 1 | -9.65392 | 3.29961 | -2.93 | 0.0044 |
| RuleofLaw | RuleofLaw | 1 | 11.38286 | 3.99629 | 2.85 | 0.0055 |

According to the analysis, the value of R-squared is 0.4136. In other words, 41.36% of variance is explained in the regression analysis. The values of F-test is 0.0001. For this reason, it can be said that the fit of model is reliable.

In the regression analysis, P value for the causal relationship between duration of government and concessional loan is 0.0166 which indicates that the variables reject the null hypothesis and the effect is statistically significant at 0.05 level. The impact of concessional loan on the government incumbency is positive and robust to regression models both with and without control variables for the case of Mongolia.

It is important to note, that the control variables provide useful insight. In particular, party affiliation has a positive impact on the duration of the government, as well as whether the government is consisted of single party

or more than 2 parties. Increase of consumer price index positively impacts the duration of the government. Moreover, foreign direct investment, which is representing the business environment, has a very low negative impact on the duration of government. About the WGI indices, political stability and absence of violence index impacts positively on duration of government. Same result showed on rule of law index. However, regulatory stability shows negative impact to duration of government while used together with other variables.

4.2. Discussion

The regression analysis results provide interesting insight into the effect that foreign concessional loan has on the duration of the government. Due to the increasing number of concessional loan that is a main contributor to the government debt, I wanted to see how concessional loan effects government duration which is to say quite short in Mongolia. In order to gain deeper insight into the hypothesis I used control variables to the analysis and the result shows a noteworthy story that has strong policy implications.

Regardless of the foreign concessional loan, the outstanding amount creates a positive impact on duration of Government of Mongolia. This could mean that the concessional loan increase can extend the duration of government. In other words, government borrows more concessional loan from donors

to stay longer and incumbent.

As discussed in chapter 2, development partners lend their money mainly to the countries which have stable politics and favorable economic situation. According to the statement made by Wenli Lu, in many developing countries, a change in government ends to change the policy for foreign environment. Political risk goes beyond government stability, because even a stable government could react to criticisms or threats and create an environment and policies unfavorable to international lending operations (LuWenli, 2003). If the government takes right policy measures and keeps economic situation positively and government stable, then the donors tend to lend more concessional loan and government itself can benefit from a development lending operation.

Borrowing concessional loan from development partners may seem like very good opportunities followed by many positive effects and impacts. To test the effectiveness of ODA, Wenli Lu did analysis on the effectiveness of IDA¹¹ financed projects and the result showed that 50% of project outcome is unsatisfactory and substantial impact on development is only 29% (LuWenli, 2003) which is quite low while the financial source is needed to be paid back with the interest.

¹¹ IDA, International Development Association, is one of the financial organization of World Bank Group.

Not only ineffectiveness, Djankov, Montalvo, and Reynal-Querol found that ODA has a negative impact on poor countries because of the large dependency governments have on the capital (Djankov, Simeon, Jose G. Montalvo, Marta Reynal-Querol, 2008). In this study, the Low-income countries displayed lower GDP growth and an average ODA as a ratio of GDP of 16%, and it's likely a much higher percentage of the respective government budget as well. This practically means that ODA including grant and loan does not give much positive impact on the growth and economy of developing and underdeveloped countries.

While ODA is not efficient enough, government borrows more concessional loan for donors. The reason can be to stay in power longer, and to implement and finance their action plan with the source of ODA for the purpose of their next successful election. It may show positive result in a short term, however, in the long run, government debt will increase which can lead to possible "Debt Trap Diplomacy".

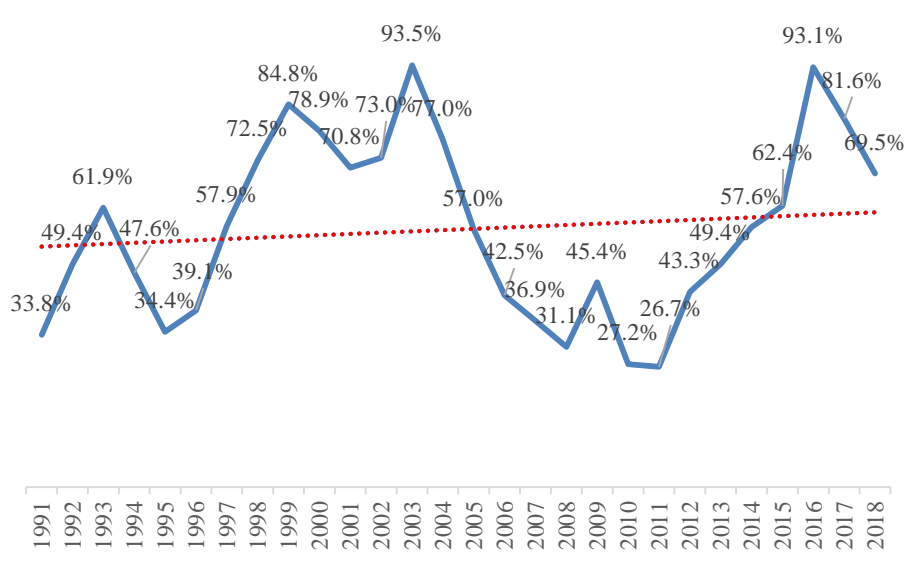
As discussed in chapter 2, Debt trap is becoming a concern for developing countries in the modern days. With the support of ODA, namely very few countries, such as South Korea, Estonia and Czech Republic, could shift from recipient country to donor country since 1960's when ODA had become a major financial source for development. However, the rest of the countries, total 133 underdeveloped and developing countries, are still a

recipient of ODA and lies in a poverty. Even some countries started losing their land to the donors due to the inability of their repayment even though the loan term is concessional. For example, through the BRI project, defaulters have been pressured by China into surrendering assets and territory or allowing military bases on their land. Sri-Lanka built CM port with the support of China's BRI projects. But the country failed to pay their loan back. Owing more than USD 1 billion in debts to China, Sri-Lanka handed over a port to companies owned by Chinese government on a 99 year lease. Small country like Tonga also carries out some big debts to China and the amount is equal to quarter of a country's GDP. China is taking over Zambia's international airport after a debt instalment default, while Congo is in deep debt due to China-funded projects. Many of these projects are linked to the "Belt and Road Initiative", a bold project to create trade routes through huge swathes of Eurasia with China at the center. Participating countries are supposed to undertake works on roads and ports from China for development, however it turned out to be their loss.

We cannot expect the same could happen to Mongolia in the future. Mongolia has borrowed concessional loan from many donor countries and organizations, and the debt level has reached very high and became a critical issue to the nation. The graph 4.1 for debt to GDP ratio shows that the trend is slightly been increasing in Mongolia. The debt to GDP ratio is a bit below the limit set by the Debt Management law of Mongolia which

was newly adopted in 2015. Even though the debt limit is set by the law, it can be amended year to year depending on the debt level by the authorized institution which is the parliament as proposed by the government.

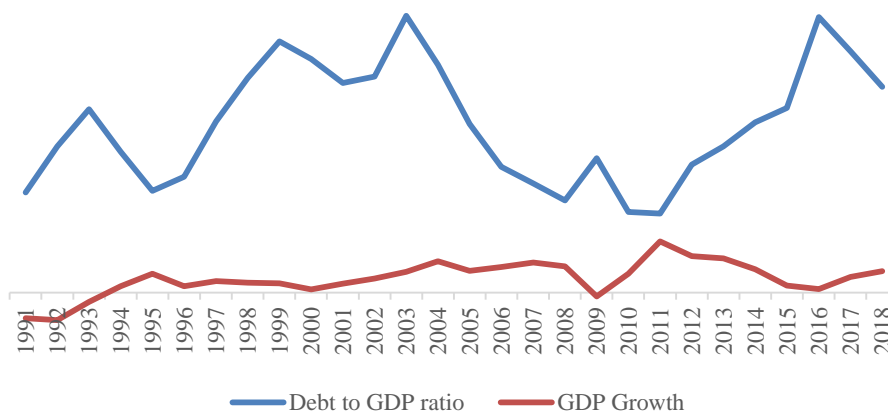
Graph 4. 1. Government Debt to GDP ratio from 1991-2018 /percentage/



Source: Ministry of Finance of Mongolia

The debt level was lower at 26.7% of GDP in 2011 when the economic growth was at peak, but increased when the economy got worsened in 2014-2016. The graph 4.2 shows the comparison of the fluctuation of GDP growth and debt to GDP ratio.

Graph 4. 2. Comparison of GDP Growth and Government Debt to GDP ratio from 1991-2018



Source: National Statistics Office and Ministry of Finance of Mongolia

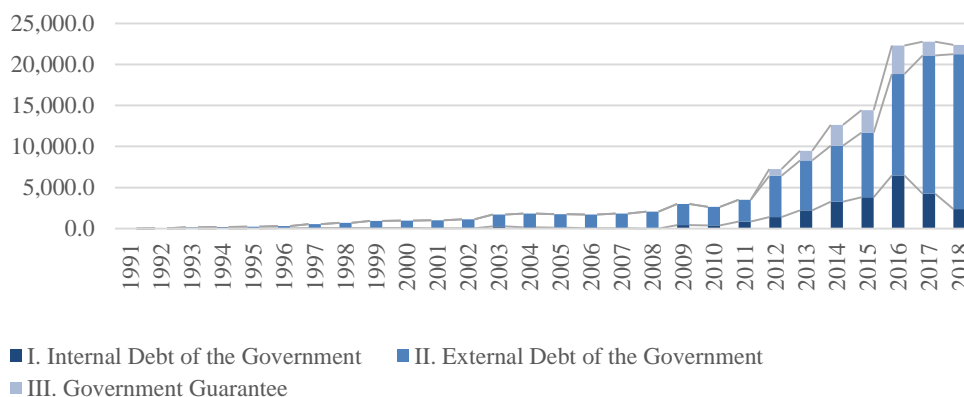
According to the graph, GDP growth and Government Debt to GDP ratio have negative relationships. When economy does better and the economic environment improves, the debt to GDP ratio goes down. The reason can be either the increase of gross domestic product or the decrease in debt amount which can be repaid and regulated according to the contract signed with the investors. Debt amount decreases not because country pays a whole lot amount to the lenders but because country borrows less money during the economic development.

In graph 4.3, the graph of the debt structure of Mongolia is shown historically from 1991 to 2018. Since 1991, external sources have been covering most of the debt and, starting from 2009, the Government of

Mongolia has begun to create debts internally which includes internal bonds, internal loans from banks, bills and notes, concession/PPP and tax advances. But, the external sources still take a huge role with 84% as of 2018 in the structure of the debt.

The government debt has reached 69.5% of GDP as of 2018. This number may look no problem to developed countries like Japan or USA, the countries with the high amount of debt in the world with 238% and 106% of GDP. However, the debt created by those developed countries are internally borrowed loans which is nothing to do with debt trap issue. But, in the case of Mongolia, 84% of total government debt¹² is externally borrowed sources, including concessional loan and foreign bonds.

Graph 4. 3. Government Debt Structure / in MNT¹³ billion/



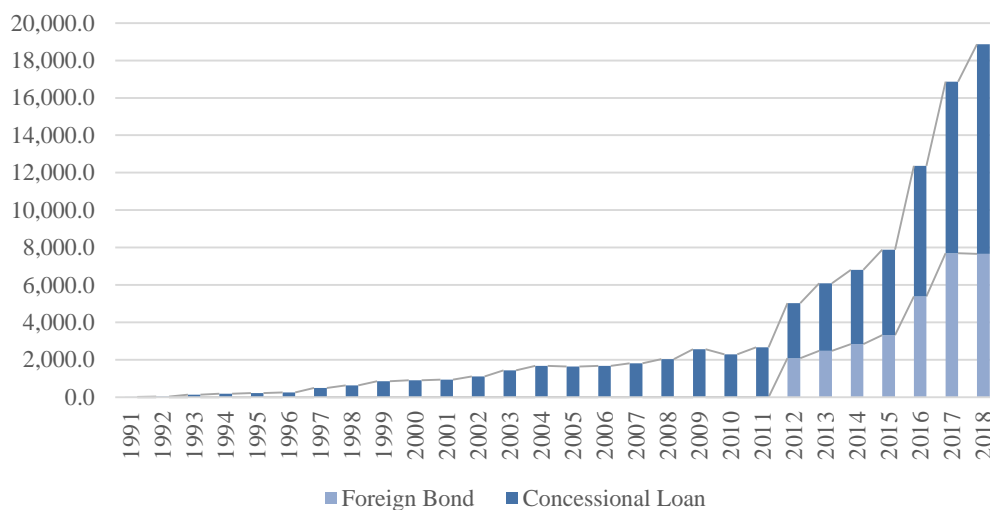
Source: Ministry of Finance of Mongolia

¹² The detailed data of government debt is shown in appendix D.

¹³ MNT-The national currency of Mongolia, Tugrug. Exchange rate ratio with

Concessional loan accounts 59% of total external debt as of 2018. The graph 4.4, the structure of the external sources are shown extensively.

Graph 4. 4. Structure of External Debt /in MNT billion/

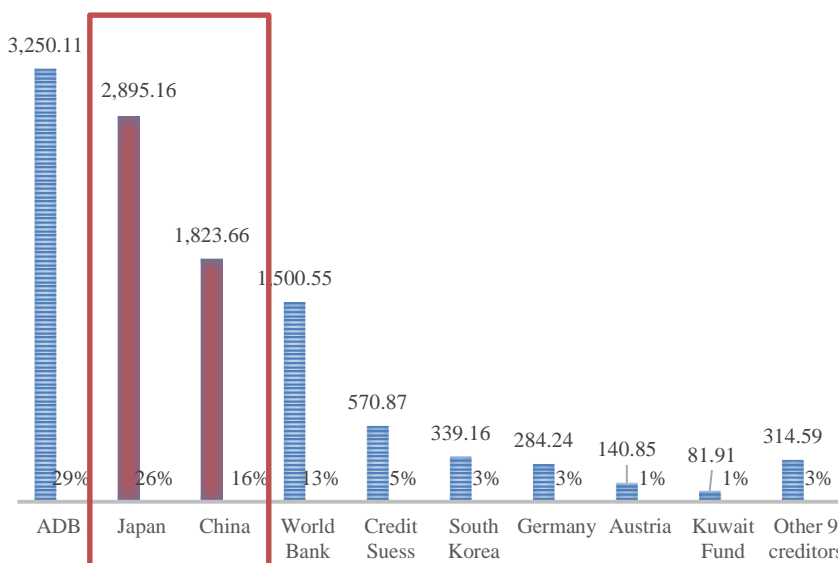


Source: Ministry of Finance of Mongolia

Concessional loan in Mongolia had borrowed the most from ADB which is a multilateral organization followed by the Government of Japan and China. The graph 4.5 shows the concessional loan outstanding of 2018 by creditors.

USD as of 2018.12.31 is 2643.69.

Graph 4. 5. Concessional Loan Outstanding as of 2018 by Donors /in MNT billion/

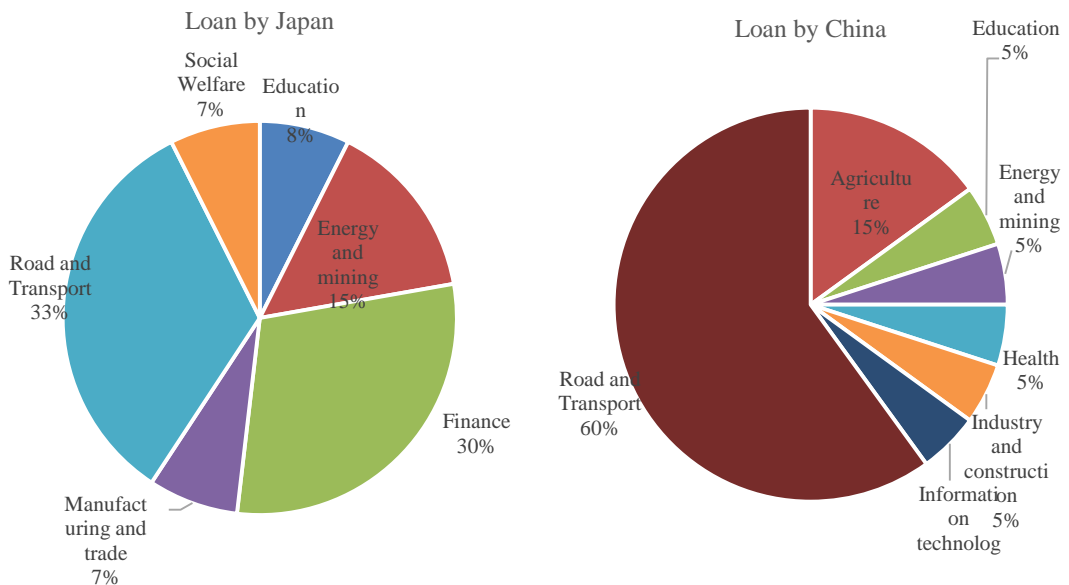


Source: Ministry of Finance of Mongolia

Multilateral donors are more responsible in terms of its implementation, regulations and monitoring. The ones taking attention are the bilateral donor countries. One of the creditor, Mongolia had borrowed the highest amount of concessional loan, is Japan which is already accounted as our honored friend country due to its ODA allocation, amount and years conducted. With Japan, Government of Mongolia had implemented total of 27 projects with average interest rate of 1.11% for average of 28.9 years since 1990. The biggest sector that Japan had invested is road and transport sector with 33% followed by financial sector with 30% and energy and mining with 15%. Comparing to Japan, Chinese lending is increasing rapidly last few years. China had invested for 20 projects with average interest rate 1.73%

with 20 year average repayment period¹⁴. The condition of loan for China is a little harder than Japan with its interest rate and repayment period. The sectors Japan and China had invested are shown in graph 4.5.

Graph 4. 6. Concessional Loan from Japan and China by Sectors from 1990-2018



Source: Ministry of Finance of Mongolia

The loan contract for 48% of Japan funded projects are signed before 2010 from 1990 to 2009 and the rest is signed from 2010 to 2018. But 80% of China's projects are signed after 2010. The concessional loan project

¹⁴ The detailed information of number of projects financed by Japan and China are shown in appendix E.

implemented by China are mostly for infrastructure sector. The debt we owe only to Japan and China together is 42% of total concessional loan and it is 29% of Mongolia's total GDP.

We cannot negate Mongolia could face similar debt trap issue like African and South Asian countries by losing the part of the country land to other country's ownership or accepting their military bases to our homeland or there can be any other consequences we cannot define currently. This is not just a debt issue. The sovereignty of a country can be taken into account in the future.

CHAPTER 5. CONCLUSION

5.1. Summary of Findings

The change of government or political instability causes many negative impacts to the economy and the society. One of the main issues is the sharp increase of government debt which may lead to “debt trap diplomacy”, some of the developing countries are facing nowadays. So that, this thesis sought to analyze the causal relationship between government incumbency and concessional loan for the case Mongolia to find whether the ODA affects the political instability.

Previous studies have investigated deeply into the conception of government incumbency and how political power affects the incumbency of the government, how incumbent government can affect to the society and the economy, what relationship the government and ODA have, and what impact ODA have on the recipient country. This study puts more stress on the role of concessional loan because loan is the main contributor to the government debt. In this respect, this study made attempts to test the hypothesis that concessional loan has a positive impact on the duration of the incumbent government, and if government borrows more concessional loan from donor countries, it will be the factor for the extension of incumbent government.

The analysis draws upon a data set of 27 years of government incumbency, and concessional loan outstanding amount of Mongolia over the period from 1991 to 2018. The control variables used in the regression models are party affiliation, coalition government, political stability and absence of violence index, regulatory quality index, rule of law index, consumer price index, and foreign direct investment amount.

The findings of the study showed that the causal relationship between two variables have positive result which indicates that concessional loan increase makes the duration of government longer and have contribution on the politics for staying more stable. In other words, we can conclude that government borrows more concessional loan from donors to stay longer in power and use the external financial sources to finance projects and activities in line with their political interests.

There are endless debates on the efficiency and the impact of ODA still going on within experts. Additionally, the study shows the facts that some projects implemented by making huge debts owed to foreign countries are inefficient after implementation, and the ODA is not necessarily an effective tool for economic growth and development of the country. The reason for inefficiency is that donor countries have their own economic interest and target the developing and poor countries with potential income or any other resources. Another reason for inefficiency is that the allocated

financing is not used efficiently where it is needed and recipient countries face to buy products at higher prices which makes the ODA result inefficient at the end.

Not only inefficiency, study also emphasizes negative impacts of ODA, including the increase of poverty and inequality, and corruption, to the recipient country. The worst is a debt trap which has become an important issue recently, because many developing countries fall into debt trap due to its inability to repay their debt back to the donor country. Due to the poor public policy, government borrows huge amount of concessional loan from foreign countries for short-sighted projects, and this makes the level of government debt increase sharply. In the long run, countries may have to face reconsideration of their sovereignty issue as a result of their poor ODA policy.

5.2. Policy Implications and Limitations

While the projects financed by ODA source show no effective results to the economy and society after implementation according to some studies stated in the literature review, the causal relationship between concessional loan and government incumbency showed positive result indicating that increase of concessional loan can extend the government duration which is a part of political stability. In that case, developing country like Mongolia may need to focus on two major policies; well regulated stable institutions and

systems, and well- formulated ODA policy.

As discussed earlier, the change of government ends to change the policy environment. The Government of Mongolia changed once in average of 1.9 years which tend to change the whole systems and policies more frequently. To aim for further growth both in economy and society, we need well-regulated stable government institutions and systems. The public institutions should be independent from political institutions in terms of its operationalization and formulation of policies which should be reached to every citizen in the country. Furthermore, to separate political activities from public institutions, government should take actions towards omitting political influence and political party membership from each individual public servants, and develop and promote attitudes towards public ethic within them.

For increasing the economic and social growth of the country and preventing from possible debt crisis, the country should have well-formulated ODA policy, especially during this time, the ODA is in demand. Mongolia is currently implementing 76 projects financed by concessional loan which has to be paid with its interest back to the donors. As shown in appendix I, 52% of outstanding amount of ongoing concessional loan projects are implemented in road and transport sector, 16% is in financial sector, and the rest of the sectors account for quite small amount. Most of

concessional loan focused on road and transport sectors that do not have direct impact on economic and social growth of the country and do not generate income, but account lots of government debt. The ODA policy and long term development policy should be linked, and government should focus on long term development of the country rather than focusing on short sight of political interests.

Although this study has policy implications based on analyzing the causal relationship between concessional loan and government incumbency, there is a limitation regarding data sets used for testing. Most data for economic, social and political indicators are available from 2000's to 2018 in yearly basis in Mongolia. Due to the lack of data availability, only 91 out of 112 selected data is estimated due to missing variables in the regression analysis.

For further studies, the extended research including and comparing other developing countries to test the causal relationship of the government incumbency and concessional loan in the broader sense may take account of multiple facets of the government. Furthermore, including different economic and political indicators for the analysis as control variables and test using different models may give more valuable explanation for the impact of ODA on government incumbency at the distinct view.

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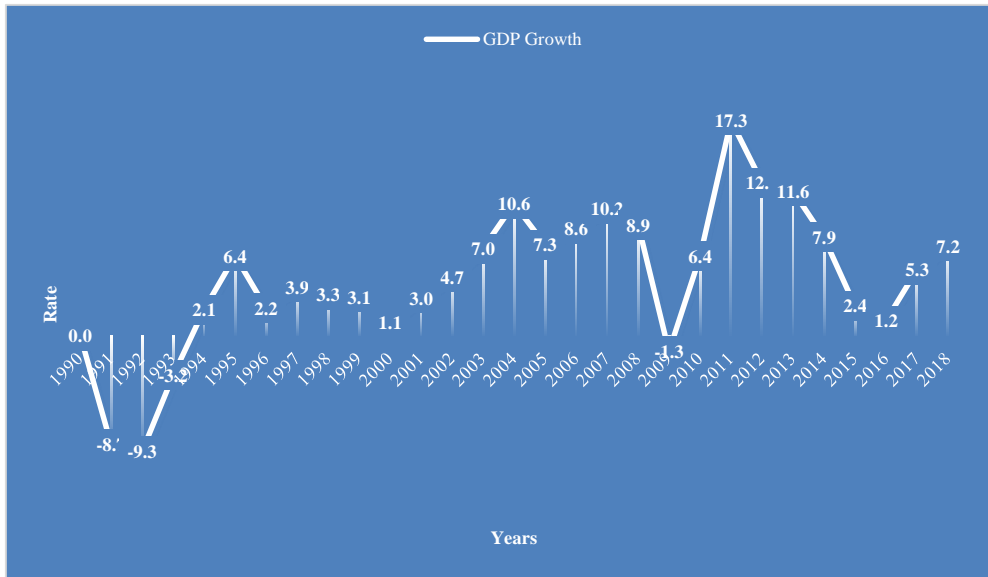
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APPENDICES

APPENDIX A

GDP GROWTH OF MONGOLIA FROM 1991-2018 /PERCENTAGE/

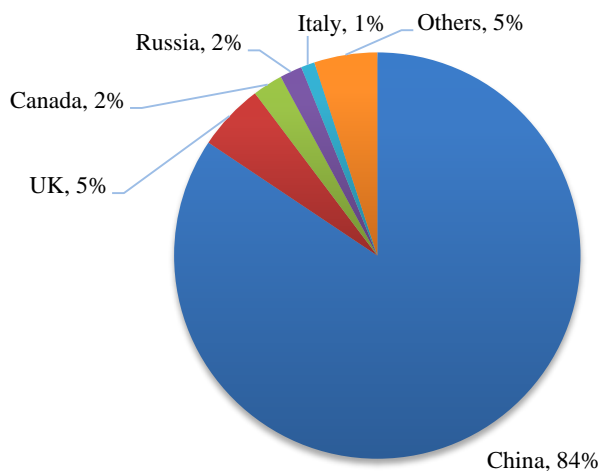


Source: National Statistics Office of Mongolia

APPENDIX B

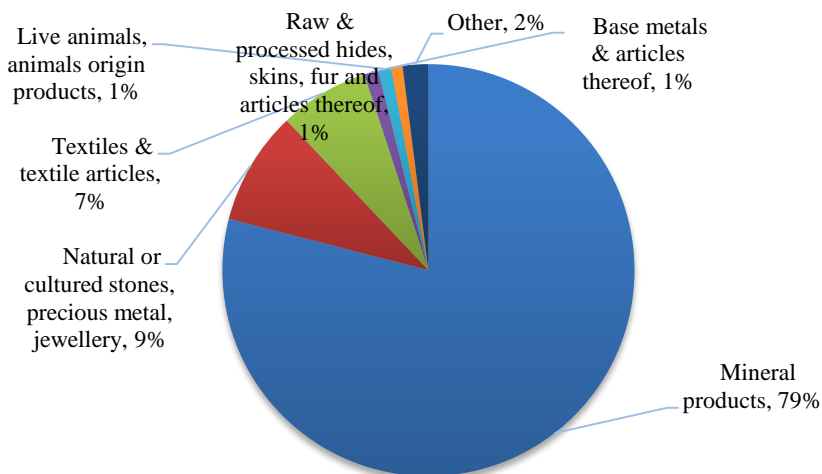
TOTAL EXPORT BY COUNTRY AND PRODUCT TYPE FROM 2005-2018

Total Export by Countries from 2005-2018 /percentage/



Source: National Statistics Office of Mongolia

Total Export by Product Type from 2005-2018 /percentage/



Source: National Statistics Office of Mongolia

APPENDIX C

GOVERNMENT INCUMBENCY PERIOD SINCE 1990

| Gov't # | Started | Terminated | Incumbency in Days | Incumbency in Years |
|---------|------------|------------|-----------------------|------------------------|
| 1 | 12/12/1984 | 3/21/1990 | 1925 | 5.3 |
| 2 | 3/21/1990 | 9/11/1990 | 174 | 0.5 |
| 3 | 9/11/1990 | 7/21/1992 | 679 | 1.9 |
| 4 | 7/21/1992 | 7/19/1996 | 1459 | 4.1 |
| 5 | 7/19/1996 | 4/23/1998 | 643 | 1.8 |
| 6 | 4/23/1998 | 12/9/1998 | 230 | 0.6 |
| 7 | 12/9/1998 | 7/22/1999 | 225 | 0.6 |
| 8 | 7/22/1999 | 7/30/1999 | 8 | 0.0 |
| 9 | 7/30/1999 | 7/26/2000 | 362 | 1.0 |
| 10 | 7/26/2000 | 8/20/2004 | 1486 | 4.1 |
| 11 | 8/20/2004 | 1/13/2006 | 511 | 1.4 |
| 12 | 1/25/2006 | 11/22/2007 | 666 | 1.9 |
| 13 | 11/22/2007 | 10/28/2009 | 706 | 2.0 |
| 14 | 10/29/2009 | 8/9/2012 | 1015 | 2.8 |
| 15 | 8/9/2012 | 10/5/2014 | 787 | 2.2 |
| 16 | 11/21/2014 | 7/30/2016 | 617 | 1.7 |
| 17 | 7/30/2016 | 9/8/2017 | 405 | 1.1 |
| 18 | 9/8/2017 | 12/31/2018 | 479 | 1.3 |

APPENDIX D

GOVERNMENT DEBT STATISTICS OF MONGOLIA FROM 1991-2018 /MNT BILLION/

| Structure | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|------------|-------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|----------------|----------------|----------------|----------------|----------------|
| I. Government Internal Debt | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 28.8 | 52.8 | 63.8 | 60.3 | 64.7 | 44.6 | 30.9 | 269.0 | 142.5 | 98.3 | 38.2 |
| 1.1 Bonds | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 28.8 | 52.8 | 63.8 | 60.3 | 64.7 | 44.6 | 30.9 | 269.0 | 142.5 | 98.3 | 38.2 |
| 1.2 Loan | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| 1.2 Securities and Bills | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| 1.3 Concession | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| 1.4 Tax advance | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Debt issued by State Owned Enterprises | | | | | | | | | | | | | | | | |
| II. Government External Debt | 7.6 | 27.7 | 141.0 | 181.7 | 224.1 | 260.0 | 487.3 | 621.8 | 856.5 | 901.6 | 940.9 | 1,101.1 | 1,441.6 | 1,674.8 | 1,635.8 | 1,672.7 |
| 2.1 Bonds | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| 2.2 Concessional Loan | 7.6 | 27.7 | 141.0 | 181.7 | 224.1 | 260.0 | 487.3 | 621.8 | 856.5 | 901.6 | 940.9 | 1,101.1 | 1,441.6 | 1,674.8 | 1,635.8 | 1,672.7 |
| III. Guaranteed Debt | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Government | | | | | | | | | | | | | | | | |
| 3.1 Debt | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Guarantee | | | | | | | | | | | | | | | | |
| TOTAL GOVERNMENT DEBT (I+II+III) | 7.6 | 27.7 | 141.0 | 181.7 | 224.1 | 288.9 | 540.1 | 685.6 | 916.8 | 966.3 | 985.5 | 1,132.0 | 1,710.7 | 1,817.3 | 1,734.1 | 1,710.9 |
| Debt Ceiling set by the Law | | | | | | | | | | | | | | | | |
| Debt/GDP | 33.8% | 49.4% | 61.9% | 47.6% | 34.4% | 39.1% | 57.9% | 72.5% | 84.8% | 78.9% | 70.8% | 73.0% | 93.5% | 77.0% | 57.0% | 42.5% |

Source: Ministry of Finance of Mongolia, National Statistics Office of Mongolia

APPENDIX D (continued)

GOVERNMENT DEBT STATISTICS OF MONGOLIA FROM 1991-2018 /MNT BILLION/

/MNT billion/

| Structure | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|----------------|----------------|----------------|----------------|----------------|----------------|----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| I. Government Internal Debt | 21.8 | 1.5 | 422.2 | 368.5 | 852.4 | 1,395.1 | 2,222.2 | 3,277.8 | 3,800.0 | 6,464.9 | 4,230.1 | 2,370.7 |
| 1.1 Bonds | 21.8 | 1.5 | 278.2 | 180.0 | 503.3 | 1,009.6 | 1,849.6 | 2,964.1 | 3,333.2 | 5,488.8 | 3,461.9 | 1,564.7 |
| 1.2 Loan | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| 1.2 Securities and Bills | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 164.3 | 307.2 | 0.0 | 0.0 |
| 1.3 Concession | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 261.0 | 668.9 | 768.2 | 806.0 |
| 1.4 Tax advance | 0.0 | 0.0 | 144.0 | 188.5 | 349.1 | 385.5 | 372.5 | 313.7 | 41.4 | 0.0 | 0.0 | 0.0 |
| Debt issued by State | | | | | | | | | | | | |
| 1.6 Owned | | | | | | | | 0.0 | 0.0 | 0.0 | | |
| Enterprises | | | | | | | | | | | | |
| II. Government External Debt | 1,807.0 | 2,037.0 | 2,570.3 | 2,289.6 | 2,665.5 | 5,023.7 | 6,094.2 | 6,807.5 | 7,881.2 | 12,363.8 | 16,857.8 | 18,865.6 |
| 2.1 Bonds | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 2,088.2 | 2,481.2 | 2,828.4 | 3,315.8 | 5,380.5 | 7,701.6 | 7,664.5 |
| 2.2 Concessional Loan | 1,807.0 | 2,037.0 | 2,570.3 | 2,289.6 | 2,665.5 | 2,935.5 | 3,613.1 | 3,979.1 | 4,565.4 | 6,983.3 | 9,156.2 | 11,201.1 |
| III. Guaranteed Debt | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 807.4 | 1,160.2 | 2,544.4 | 2,743.5 | 3,451.5 | 1,663.7 | 1,130.7 |
| Government | | | | | | | | | | | | |
| 3.1 Debt | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 807.4 | 1,160.2 | 2,544.4 | 2,743.5 | 3,451.5 | 1,663.7 | 1,130.7 |
| Guarantee | | | | | | | | | | | | |
| TOTAL GOVERNMENT DEBT (I+II+III) | 1,828.8 | 2,038.5 | 2,992.5 | 2,658.0 | 3,517.9 | 7,226.2 | 9,476.6 | 12,629.7 | 14,424.7 | 22,280.1 | 22,751.6 | 22,367.0 |
| Debt Ceiling set by the Law | | | | | | | | | 58.3% | 88.0% | 85.0% | 80.0% |
| Debt/GDP | 36.9% | 31.1% | 45.4% | 27.2% | 26.7% | 43.3% | 49.4% | 57.6% | 62.4% | 93.1% | 81.6% | 69.5% |

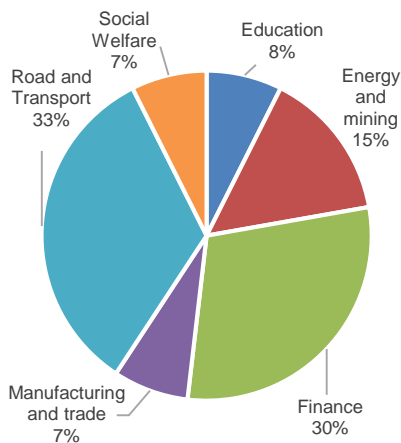
Source: Ministry of Finance of Mongolia, National Statistics Office of Mongolia

APPENDIX E

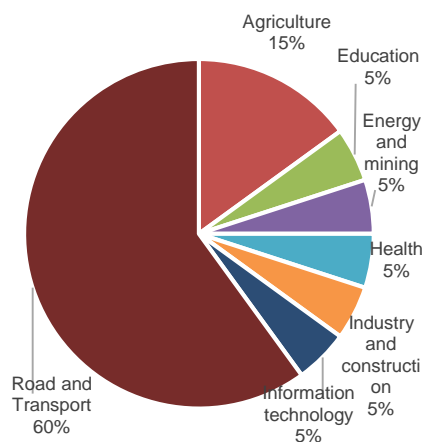
NUMBER OF PROJECTS FINANCED BY GOVERNMENT OF JAPAN AND CHINA FROM 1991-2018

| | |
|---------------------------|-----------|
| China | 20 |
| Agriculture | 3 |
| Education | 1 |
| Energy and mining | 1 |
| Health | 1 |
| Industry and construction | 1 |
| Information technology | 1 |
| Road and Transport | 12 |
| Japan | 27 |
| Education | 2 |
| Energy and mining | 4 |
| Finance | 8 |
| Manufacturing and trade | 2 |
| Road and Transport | 9 |
| Social Welfare | 2 |
| Grand Total | 47 |

Loan by Japan



Loan by China



Source: Ministry of Finance of Mongolia

APPENDIX F

CONCESSIONAL LOAN OUTSDANDING AMOUNT BY DONOR AS OF 2018 /MNT BILLION/

| Creditor | Amount |
|-------------------------|------------------|
| China | 3,250.11 |
| Sweden | 2,895.16 |
| Belgium | 1,823.66 |
| Germany | 1,500.55 |
| Kuwait Fund | 570.87 |
| IFAD | 339.16 |
| Credit Suesse | 284.24 |
| Japan | 140.85 |
| India | 81.91 |
| Abu-Dabi Fund | 74.36 |
| Spain | 67.95 |
| Nordic Development Fund | 65.55 |
| France | 43.72 |
| South Korea | 21.15 |
| Austria | 14.11 |
| World Bank | 13.90 |
| ADB | 10.49 |
| EIB | 3.35 |
| Total | 11,201.12 |

Source: Ministry of Finance of Mongolia

APPENDIX G

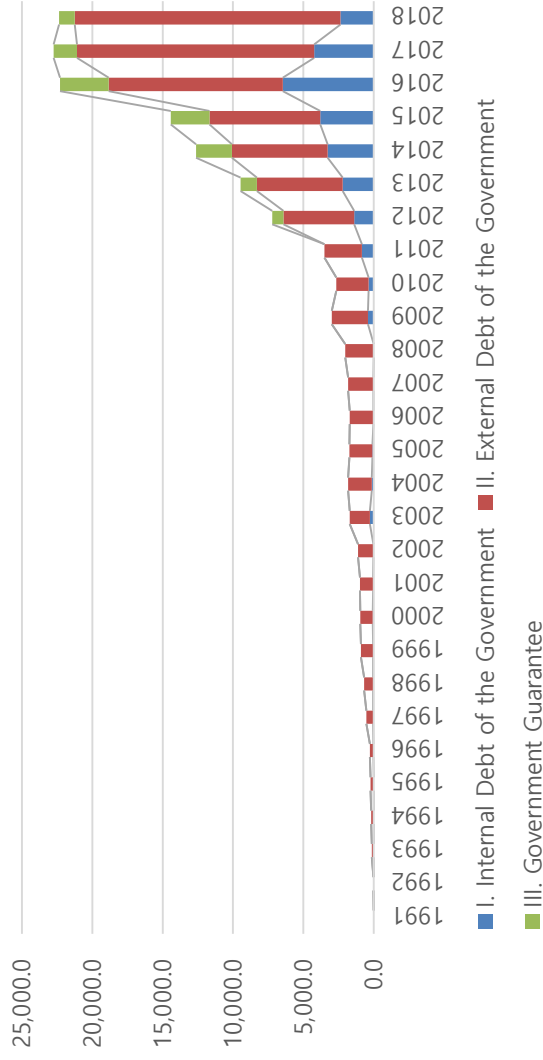
GOVERNMENT DEBT BY PERCENTAGE

| Debt Structure | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
|-------------------------------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| I. Internal Debt of the Government | 0% | 0% | 0% | 0% | 0% | 10% | 10% | 9% | 7% | 7% | 5% | 3% | 16% | 8% |
| II. External Debt of the Government | 100% | 100% | 100% | 100% | 100% | 90% | 90% | 91% | 93% | 93% | 95% | 97% | 84% | 92% |
| III. Government Guarantee | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% |

| Debt Structure | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|-------------------------------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| I. Internal Debt of the Government | 6% | 2% | 1% | 0% | 14% | 14% | 24% | 19% | 23% | 26% | 26% | 29% | 19% | 11% |
| II. External Debt of the Government | 94% | 98% | 99% | 100% | 86% | 86% | 76% | 70% | 64% | 54% | 54% | 55% | 74% | 84% |
| III. Government Guarantee | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 11% | 12% | 20% | 19% | 15% | 7% | 5% |

Source: Ministry of Finance of Mongolia

APPENDIX G (continued)
GOVERNMENT DEBT BY PERCENTAGE



Source: Ministry of Finance of Mongolia

APPENDIX H

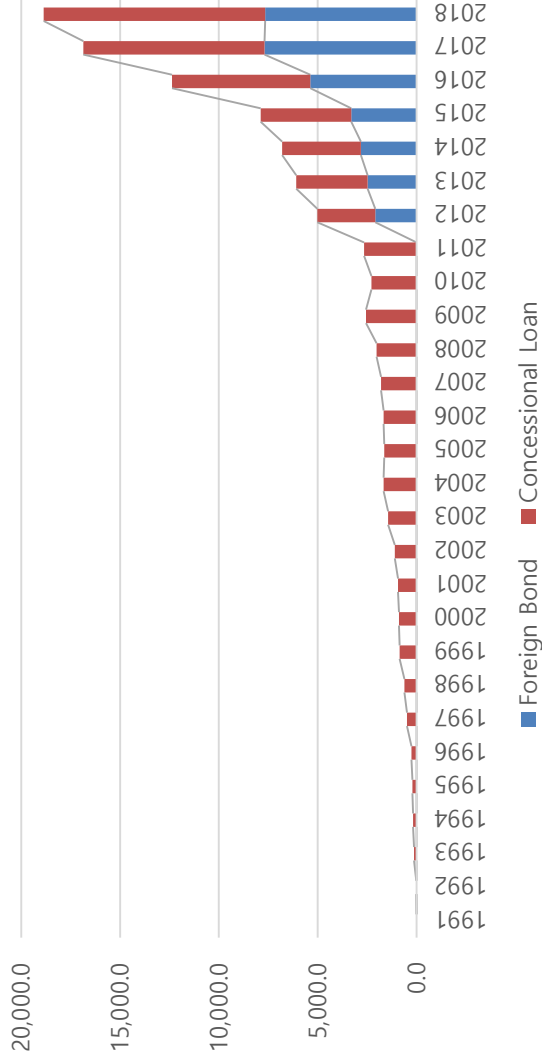
EXTERNAL DEBT BY PERCENTAGE

| | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 |
|-------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| <i>Bond</i> | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| <i>Loan</i> | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |

| | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|-------------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| <i>Bond</i> | 0% | 0% | 0% | 0% | 0% | 0% | 42% | 41% | 42% | 42% | 44% | 46% | 41% |
| <i>Loan</i> | 100% | 100% | 100% | 100% | 100% | 100% | 58% | 59% | 58% | 58% | 56% | 54% | 59% |

Source: Ministry of Finance of Mongolia

APPENDIX H (continued)
EXTERNAL DEBT BY PERCENTAGE



Source: Ministry of Finance of Mongolia

APPENDIX I

THE PERCENTAGE OF CONCESSIONAL LOAN OUTSTANDING AMOUNT BY SECTOR /1990-2018/

| Sector | Percentage |
|---|-------------------|
| Finance | 36% |
| Road and Transport | 32% |
| Energy and Mining | 8% |
| Social Welfare | 4% |
| Health | 4% |
| Agriculture | 3% |
| Water Supply, City Infrastructure and Service | 3% |
| Education | 3% |
| Information and Technology | 3% |
| Industry and Construction | 2% |
| Trade | 1% |
| Justice and Regulation | 1% |

THE PERCENTAGE OF CONCESSIONAL LOAN OUTSTANDING AMOUNT BY SECTOR /ONGOING PROJECTS/

| Sector | Percentage |
|---|-------------------|
| Road and Transport | 52% |
| Finance | 16% |
| Health | 7% |
| Industry and Construction | 5% |
| Agriculture | 5% |
| Education | 5% |
| Energy and Mining | 4% |
| Water Supply, City Infrastructure and Service | 3% |
| Information an Technology | 2% |
| Social Welfare | 1% |
| Justice andd Regulation | 0% |
| Trade | 0% |

Source: Ministry of Finance of Mongolia

국문초록

양허성 차관이 정부의 재임기간에 미치는 영향: 몽골 사례를 중심으로

Undrakh Lkhagvasuren

서울대학교 행정대학원

글로벌행정전공

본 논문은 몽골의 외국의 양허성 차관과 정부 재임기간과의 인과관계를 규명하고자 한다. 그 결과, 다중 회귀분석을 이용해 두 변수 사이의 인과관계를 보면 양허성 차관이 늘어나면 현 정부가 더 오래 머무를 수 있다는 긍정적인 결과가 나타났다. 결론은 정부가 장기 집권을 위해 공여국으로부터 더 많은 양허성 차관을 얻고 그들의 정치적 이익에 부합하는 프로젝트에 자금을 대기 위해 외국 차관을 사용한다는 것이다.

게다가, 문헌 조사에서는 외국의 양허성 차관으로 자금을 조달하는 일부 프로젝트는 비효율적이고 공적개발원조(ODA)는 경제성장과 국가의 발전에 효과적인 수단이 아니라는 사실을

설명한다. 비효율적인 이유는 공여국들이 그들 자신의 경제적 이익을 가지고 있고 그들의 필요에 따라 그 이익을 목표로 삼기 때문이다. 또한, 할당된 자원은 필요한 곳에서 효율적으로 사용되지 않고, 수원국들은 더 높은 가격으로 제품을 구입하기 때문에, 결국 공적개발원조 프로젝트 결과는 비효율적이다.

비효율적인 것뿐만 아니라, 본 논문에서 공적개발원조의 부정적 영향에 대해서도 논의하였다. 가장 나쁜 것은 최근 몽골을 포함한 개발도상국들에게 중요한 이슈가 되고 있는 것은 채무 함정인데, 많은 개발도상국들이 공여국에게 채무를 갚지 못해 채무의 함정에 걸려 있기 때문이다. 정부가 만든 부실 공적개발원조의 정책 때문에 국가들의 대외채무가 급증하고 주권국가들은 독립성을 재고해야 할 처지에 놓여있다.

주제어: 공적개발원조(ODA), 양허성 차관, 정부 재임기간, 국가채무

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